Third-Party Funding of International Arbitration

Being a Presentation By

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Introduction

Over the years, Nigerian entities have entered into various contractual relationships. Thus in attracting foreign direct investments, various contractual or treaty relationships have developed. Conventionally disputes arising from such economic activities were settled by litigation. However, the new trend is arbitration.

Arising from these relationships, there are disputes involving Ministries, Departments and Agencies (MDAs). There are also disputes involving small and middle-sized companies. These entities may not have the resources to fund these arbitration costs. The trend now in Europe and Americas is Third Party Funding of International Arbitration. This is closely related to the controversial phenomenon of third party funding in litigation.

In this presentation, we are not concerned with third party funding of litigation nor with domestic arbitration but third party funding of international arbitration.

Types of Arbitration

Arbitration can be *ad hoc* or institutional – an arbitration is *ad hoc* if not administered by any arbitral institution like the Rules of Arbitration of the International Chamber of Commerce, London Court of International Arbitration, American Arbitration Association, Stockholm Chamber of Commerce Arbitration Rules, among others. It is institutional if administered by any of these arbitral institutions.

Arbitration can also be domestic or international. It is domestic if the parties to the arbitration agreement have at the time of the conclusion of the agreement their places of business in the same country. In this presentation, the focus is not on domestic arbitration.

When is an arbitration is international? Section 57(2) of the Arbitration and Conciliation Act, 2004 (ACA) provides that an arbitration is international if

(a) the parties to an arbitration agreement have, at the time of the conclusion of the agreement, their places of business in different countries; or

(b) one of the following places is situated outside the country in which the parties have their places of business –

  (i) the place of arbitration if such place is determined in, or pursuant to the arbitration agreement,

  (ii) any place where a substantial part of the obligation of the commercial relationship is to be performed or the place with which the subject matter of the dispute is most closely connected; or

(c) the parties have expressly agreed that the subject matter of the arbitration agreement relates to more than one country; or

(d) the parties, despite the nature of the contract, expressly agreed that any dispute arising from the commercial transaction be treated as an international arbitration.

Laws Applicable to International Arbitration

When an arbitration is foreign or international at least five laws are applicable.

- Law determining the capacity to contract
- Law Governing the Contract
- Law Governing the Arbitration Clause – principle of separability
- Law Governing the Place of Arbitration
- Law Governing the place of enforcement

Cost of Arbitration

Section 49(1) of the ACA provides that the arbitral tribunal shall fix costs of arbitration in its award and the term 'cost' includes

(a) the fees of the arbitral tribunal to be stated separately as to each arbitrator and to be fixed by the tribunal itself;
(b) the travel and other expenses incurred by the arbitrators
(c) the costs of expert advice and of other assistance required by he arbitral tribunal;
(d) the travel and other expenses of witnesses to the extent that such expenses are approved by the arbitral tribunal;
(e) the costs for legal representation and assistance of the successful party if such costs were claimed during the arbitral proceedings, and only to the extent that the arbitral tribunal determines that the amount of such costs is reasonable.

Subsection (2) of section 49 provides that the fees of the arbitral tribunal shall be reasonable in amount taking into account the amount in dispute, the complexity of the subject-matter, the time spent by the arbitrators and any other relevant circumstances of the case.

Determination of Fees

In *ad hoc* arbitration, the arbitral tribunal determines the fees and in institutional arbitration, the arbitral institution determines the fees.

Fees can be based on the amount in dispute or on a daily or hourly rate.

Unfortunately, international commercial arbitration is becoming very expensive in terms of fees paid to arbitrators, costs of hiring venues, legal fees, witnesses – expert and fact, interpreters, transcribers, transportation and hotel costs. The arbitral awards are also alarming. For instance some arbitrators earn as much as GBP5,000 a day or GBP500 per hour. Arbitrators can fly first class or business class and flight time is paid for. Sums as high as $2 billion have been awarded. I know a Nigerian entity that has a cumulative award of $10 billion against it.

In other jurisdictions – United Kingdom, Australia, United States America and South Africa, the concept of Third Party Funding of International Arbitration is being used to minimize the adverse effects of international arbitration.

How does Third Party Funding Work:

- Third party funding is a financial model in which an entity that is not a party to a particular dispute funds another party's legal fees or pays an order, award, or judgment

rendered against that party, or both. The agreement between the funder and the funded party may also include paying another party's attorney fees if the funded party loses the case or the decision-maker (judge, arbitrator) orders the funded party to pay the attorney fees of another party.

- Jurisprudence, academic literature and other articles relating to third party funding in most jurisdictions largely focus on litigation funding, which represents the majority of third party funding instances worldwide. In Nigeria, Lucius Nwosu, SAN has done many such cases in the area of litigation in Port Harcourt.
- Third party funding in arbitration depart from the general character of litigation funding. The party seeking third party funding may be asked by the funders to provide detailed information about the transaction. Such information may be confidential or privileged under applicable law. The funder will analyse the information to determine the strengths and weaknesses, the likelihood of success and the ability to recover from the losing party. If acceptable, the client would negotiate a funding agreement – may cover the costs of the client and the other party's attorney.
- A funder may be the client's attorney or law firm, an insurance company or an outside institution such as a corporation, bank or other financial institution. In countries like Australia, Germany, the UK, Canada,

Netherlands, South Africa, New Zealand and the USA where third party funding is well developed, there are specialized funding institutions.

- Attorney financing is quite common in the form of *pro bono*, contingency, conditional or success fee arrangements. In the case of an institution that has no connection with the client, such institution may provide a traditional loan or non-recourse funding. **Non-recourse funding is the basic scenario of third party funding in international arbitration envisaged here**. On its face, it resembles contingency fee arrangement except that the funder is an outside entity such as a bank or financial institution. The institution is not constrained like the conventional and ethical rules of the attorney. Even when there is a funder, an attorney is still retained separately from the funding agreement.
- A typical funding agree will include methods for calculating the maximum amount of money the funder will contribute to the legal representation, the portion of the return that the funder will expect to receive upon success, and the maxim adverse costs award that the funder would pay, if any, in the event that the client loses the case.
- Litigation funding is available in most common law jurisdictions in the United States. The process is most commonly used in personal injury cases, but may also apply to commercial disputes, insolvency cases, civil rights cases, workers' compensation, and structured

settlement. The amount of money that plaintiffs receive through legal financing varies widely, but often is around 10 to 15 percent of the expected value of judgment or settlement of their personal injury lawsuit. Some companies allow individuals to request more or less money (as needed) and have varying payout rates depending on the characteristics of the case at hand.

Driving Forces

- Certain factors are the main driving forces in the demand for third party funding – the maxim *ubi jus ubi remedium*is the cardinal principle underlying our jurisprudence and by extension the very justification of the profession to which we belonged
- Public policy on access to justice. Should citizens be denied access to justice because of their financial standing?
- In arbitration the high values of the claims, speed of proceedings, reduction in evidentiary costs, greater predictability of outcome and enforcement regime especially under the 1958 NY Convention.

Ethical Considerations

- Attorney's professional ethics rules.
- International commercial arbitration requires parties and arbitral tribunal to comply with mandatory procedural rules

of the seat of arbitration and a court at the seat may decide to impose its view on the validity or desirability of third party funding agreement during a proceeding to recognize, enforce, annual, set aside the award.

- Similarly a court at the place of enforcement of such agreement may raise a public policy issue.
- Above all, is third party funding valid and enforceable in all jurisdictions.
- Maintenance and Champerty are the most widespread and long-standing doctrines that may serve to constrain the existence or validity of any individual third party funding agreement.

Doctrines of Maintenance and Champerty –

- Maintenance is the funding of litigation by a third party who is a stranger to the dispute. champerty is the funding of a litigation by a stranger third party in exchange for a percentage of the win. Thus champerty is an aggravated form of maintenance. The distinguishing feature of champerty is the support of litigation by a stranger in return for a share of the proceeds.
- At common law, both are illegal for two basic public policy reasons - desirable to curb excess litigation for the operation of an efficient judicial system; and bringing money to an individual who was not personally harmed by the defendant.

- In some jurisdictions, the doctrines are obsolete and prefer newer ones aimed at preventing ‘abuse of process’ and ‘malicious prosecution’ both of whom deal with the wrongful initiation of litigation and perversion of legal process. Some see maintenance and champerty as archaic and anachronistic?
- In a country like Nigeria with the level of poverty; paucity of funds and low level of access to justice in the face of breaches of contracts and inability to ventilate the grievances, should we continue to adopt the doctrines?

Attorney-Client Privilege

- Possible waiver of the attorney-client privilege when the client discloses privileged information to a potential third party funder.
- In Nigeria, Rule 17(3)(b) of the Rules of Professional Conduct for Legal Practitioners (RPC) allows for a reasonable contingent fee in civil cases.
- Rule 19 of RPC provides for Privilege and confidence of client. Thus all oral or written communications made by a client to his lawyer in the normal course of professional employment are privileged.
- Similarly under section 192 of the Evidence Act, 2011, professional communication between client and legal practitioner are privileged.

- Under section 195 of the Evidence Act, confidential communication between a client and a legal practitioner is privileged.

Interaction of different legal systems – Claimant's, Respondent's, Each of the three Arbitrators, and that of the third party funder

Lessons from other Jurisdictions

- In the **United Kingdom (UK)**, the tort and criminal laws pertaining to the doctrines of champerty and maintenance have been abolished but the common law doctrines of champerty and maintenance still apply to funding agreements, and extend to private dispute resolution methods, such as arbitration. However, third party funding is well developed in the UK.
- Under the Code of Conduct for Litigation Funders (including Arbitration), the Funder undertakes not to take any steps that cause or are likely to cause the litigant's solicitor or barrister to act in breach of their professional duties.
- In the **United States** (US), the doctrines are used to weigh the propriety or otherwise of a funding arrangement. It is still evolving in the US. Similarly, third party funding is still fraught with uncertainty in the US but funding for consumer disputes such as personal injury claims and other small claims exist. US is known for

contingency fees arrangement but the attorney must make proper disclosures to the client

- In **Australia**, the courts have declined to outline a broad rule. Counsel in cases challenging a litigation funding agreement on grounds of abuse of process and public policy are free to use wide-ranging and creative legal arguments in favour of one side or the other. Third party funding is well developed in Australia

- In **South Africa**, over time the doctrines received little to no attention and currently appear to not stand as a road block to a developing third-party funding market. Thus it appears that litigation funding has quietly become part of the South Africa landscape, getting little to no resistance in the face of what used to be portrayed as champertous agreements.

Challenges to Third Party Funding

- Potential waiver of attorney-client privilege if the funding is done by a lawyer or a law firm or where the third party funding ask for certain information about the relationship with the attorney.
- Potential encouragement of non-meritorious claims
- Possible discouragement of settlement in favour of fighting for a larger recovery
- Potential use of legal systems for financial speculation

- The risk that funder may put its own interests ahead of the client's interests
- Potential conflicts of interest that may arise if the funder meddles in the attorney-client relationship
- Whether the existence of a funding agreement must or should be disclosed to the judge or arbitrator
- Whether the funding of investment arbitration claims on the side of the investor or defences on the side of the host State comports with the spirit of the investor-State dispute resolution system.

Conclusion

There are various activities in the oil and gas, power, mining and agricultural sectors. Our focus is on contractual or treaty relationships in these sectors. This is so because unlike litigation, in arbitration, the parties must agree to arbitrate. In litigation, you do not need any agreement to litigation. The judicial powers of a state can always be invoked where civil rights and obligations are breached.

Maintenance and Champerty are still parts of our common law heritage. In many jurisdictions the doctrines are being examined to consider whether they are still useful and relevant given the myriad of other safeguards against fraud and abuse that are embedded in legal systems today. Do we still need these doctrines especially in contractual relationships where there is inequality of bargaining powers?

In Nigeria, if the funding is to be done by a lawyer, the privileges provided in the Evidence Act and the Rules of Professional Conduct will be invoked. However, where the funder is an institution, these provisions may not apply.

Any attorney whose clients are considering working with a third party funder must be cautious and conduct thorough research on the current law in any applicable jurisdiction, especially since the law is so rapidly evolving in jurisdictions where third-party funding in litigation is growing.

In Nigeria, do we allow third party funding in international arbitration to evolve naturally or we regulate it? In England there is the Association of Litigation Funders of England and Wales. The Association has a Code of Conduct for members as well as Articles and Rules.

Friday, 14 March, 2014.